STATE OF NEW YORK

TAX APPEALS TRIBUNAL

In the Matter of the Petition	:	
of	:	
REFCO PROPERTIES, INC.	:	DECISION DTA No. 812292
for Redetermination of a Deficiency or for Refund of Corporation Franchise Tax under Article 9-A of the Tax Law for the Fiscal Years Ended January 31, 1985 and January 31, 1986.	:	

Petitioner Refco Properties, Inc., c/o Hyatt Corp., 200 West Madison Street, Chicago, Illinois 60606, filed an exception to the determination of the Administrative Law Judge issued on July 20, 1995. Petitioner appeared by Horwood, Marcus & Braun (Fred O. Marcus, David A. Hughes, and Jordan M. Goodman, Esqs., of counsel). The Division of Taxation appeared by Steven U. Teitelbaum, Esq. (Robert Tompkins, Esq., of counsel).

Petitioner filed a brief on exception and a reply brief. The Division of Taxation filed a brief in opposition. Petitioner's request for oral argument was denied. However, the parties were allowed to file supplemental briefs to allow them the opportunity to comment on the impact of Matter of Brooke-Bond Group (Tax Appeals Tribunal, December 28, 1995) with respect to the current case. The original due date for the issuance of this decision was June 26, 1996, i.e., six months after the date the original reply brief was received. This date was extended for forty-five days, until August 12, 1996, to allow for the filing of the supplemental briefs.

Commissioner DeWitt delivered the decision of the Tax Appeals Tribunal. Commissioner Koenig concurs.

ISSUE

Whether petitioner may claim a net operating loss deduction on its New York State corporate franchise tax return which exceeds the amount of the net operating loss deduction claimed on its Federal corporation income tax return for a taxable year.

FINDINGS OF FACT

We find the facts as determined by the Administrative Law Judge. These facts are set forth below.

STIPULATED FACTS

1. Petitioner, Refco Properties, Inc. ("Refco"), is a Delaware corporation with its principal offices located at 200 West Madison Street, Chicago, Illinois.

2. The periods in issue in this matter are the tax years ending January 31, 1985 and January 31, 1986 (hereinafter "years in issue").

3. Refco timely filed Form 1120, U.S. Corporation Income Tax Return, for the years in issue.

4. Refco timely filed New York Form CT-3, New York Corporation Franchise Tax Report ("report"), for the years in issue.

5. For Federal income tax purposes, the following amounts were available to Refco as net operating loss ("NOL") carryforwards under section 172 of the Internal Revenue Code ("Code") in each of the years in issue:

Year Ended	Amount Available as NOL Carryforward Deduction
1/31/85	$18,219,247.00
1/31/86	18,115,862.00

6. A schedule showing the amount of NOL carryforward deduction ("NOLD") available to Refco during the years in issue is as follows:

Federal NOL Deduction Analysis	Year Ended 1/31/85	Year Ended 1/31/86
FTI (Federal Taxable Income) before NOLD	$ 103,385.00	$ 677,092.00
NOLD:		
Carryforward from 1/31/78	(34,483.00)	
Carryforward from 1/31/79	(68,902.00)	
Carryforward from 1/31/79		(677,902.00)
	-0-	-0-

New York NOL Deduction Analysis	Year Ended 1/31/85	Year Ended 1/31/86
ENI (entire net income) per prior audit before NOL deduction	$1,147,539.00	$2,015,672.00
NOLD:		
Carryforward from 1/31/78	(34,483.00)	
Carryforward from 1/31/79	(68,902.00)	
Carryforward from 1/31/79		(677,092.00)
Entire Net Income per Audit	$1,044,154.00	$1,338,580.00

7. On its U.S. corporation income tax returns for each of the years in issue, Refco claimed NOL carryforward deductions under section 172 of the Code in the following amounts:

Carryforward Utilization	Year Ended 1/31/85	Year Ended 1/31/86
From 1/78 to 1/85	$34,483.00	
From 1/79 to 1/85	68,902.00	
From 1/79 to 1/86		$677,092.00

8. The amounts utilized by Refco as NOL carryforward deductions on its U.S. corporation income tax returns for each of the years in issue were less than the amounts actually available under section 172 of the Code as set forth in paragraph 5 of the stipulation of facts.

9. On its report for the taxable year ending January 31, 1985, Refco claimed a NOL carryforward deduction in the amount of $4,309,738.00.

10. The amount claimed by Refco as a NOL carryforward deduction on its report for the year ending January 31, 1985 exceeded the amount utilized by Refco as a NOL carryforward deduction on its Federal return for that year.

11. On its report for the taxable year ending January 31, 1986, Refco claimed a NOL carryforward deduction in the amount of $677,092.00.

12. The amount claimed by Refco as a NOL carryforward deduction on its report for the year ending January 31, 1986 was equal to the amount utilized by Refco on its Federal return for that same year.

13. Refco's New York taxable income before apportionment and before any NOL deduction during the years in issue exceeded its Federal taxable income before NOL deductions during this same period due to various additions to New York taxable income, including depreciation adjustments, required by Tax Law § 208(9). Refco's respective State and Federal taxable incomes before NOL deductions during the years in issue were:

Year Ended	Federal Taxable Income Before NOL	New York Taxable Income Before Apportionment and Before NOL
1/31/85	$103,385.00	$1,147,539.00
1/31/86	677,092.00	2,015,672.00

14. Upon audit, the Division of Taxation ("Division") reduced Refco's New York NOL carryforward deduction for the taxable year ending January 31, 1985 to the amount utilized by Refco on its Federal return for that same year and determined that additional tax and interest were due from Refco.

15. Refco subsequently made payment to the Division in satisfaction of the determination of additional tax and interest due.

16. Refco subsequently filed claims for refund of New York franchise tax paid for each of the years in issue.

17. On its claims for refund, Refco recomputed its New York corporation franchise tax liability for the years in issue by claiming NOL carryforward deductions in the following amounts:

NOL Deduction	Year Ended 1/31/85	Year Ended 1/31/86
From 1/78 to 1/85	$ 34,483.00	
From 1/79 to 1/85	990,804.00	
From 1/80 to 1/85	122,252.00	
From 1/80 to 1/86		$ 295,834.00
From 1/81 to 1/86		1,719,838.00

18. The amounts claimed as NOL carryforward deductions on Refco's claims for refund exceeded the Federal NOL carryforward deductions utilized by Refco on its Federal returns for the years in issue.

19. Refco's claims for refund were denied by the Division by letter dated July 23, 1993.

20. In denying Refco's claims for refund, the Division stated that a NOL deduction for New York purposes may not exceed the deduction allowed for that year for Federal income tax purposes under section 172 of the Code.

21. Refco timely protested and took exception to the Division's denial of the claims for refund by filing a petition, dated September 17, 1993, with the Division of Tax Appeals.

22. On April 25, 1994, Refco executed a Consent to Submission Without Hearing in this matter.

OPINION

In his determination, the Administrative Law Judge concluded that petitioner may not claim a New York NOL deduction which exceeded the amount of its Federal NOL deduction for the corresponding year. He stated:

> "[p]etitioner contends that 'allowed,' in the context of Tax Law § 208(9), does not mean 'utilized' but instead must be interpreted to mean the same as 'allowed' under section 172 of the Code. In effect, petitioner makes a contention similar to that made in Royal Indemnity Company v. Tax Appeals Tribunal (75 NY2d 75, 550 NYS2d 610), where the taxpayer argued that the New York NOL deduction for any taxable year is determined by applying Federal computational principles to the amounts of income or loss determined under New York law and is not limited to or dependent on the amount of the Federal NOL deduction allowed to the taxpayer for that same year. In Royal Indemnity, the court ruled, however, that the New York NOL deduction cannot exceed the amount deducted on the Federal return for the corresponding year. . . .
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> "Under Article 9-A of the Tax Law, the NOL deduction from entire net income is permitted by Tax Law § 208(9)(f). This section's description of the deduction begins with the statement that the deduction '[s]hall be presumably the same as the net operating loss deduction allowed under section one hundred seventy-two of the internal revenue code . . . ' (Tax Law § 208[9][f]; emphasis added). The starting point is clearly the Federal deduction. It is completely consistent with the normal use of the term 'deduction' to find that it means the amount of the Federal number (Matter of Lehigh Valley Industries, Tax Appeals Tribunal, May 5, 1988).

> "The limitation to the amount of the Federal NOL deduction is premised on the understanding that section 208(9)(f) was '[p]lainly intended to conform operating loss carryback and carryover practices with Federal law in order to assist new businesses and those with fluctuating incomes' (Telmar Communications Corp. v. Procaccino, 48 AD2d 189, 369 NYS2d 208). That the amount of the State loss cannot exceed the amount of the Federal loss is essential to this principle of Federal conformity. Thus, it has been well settled that the Article 9-A NOL deduction is limited to the amount of the Federal NOL deduction for the corresponding year (Telmar Communications Corp. v. Procaccino, supra; Matter of Lehigh Valley Industries, supra)" (Determination, conclusions of law "B" and "D").

Making the same argument on exception that it presented to the Administrative Law Judge, petitioner argues that Tax Law § 208(9)(f) allows a taxpayer to claim a NOL deduction equal to the amount "allowed" under section 172 of the Internal Revenue Code (IRC) and the deduction is not limited to the amount actually utilized as a deduction on the Federal tax return. The issue presented, it claims, "is nothing more than an exercise in statutory interpretation" (Petitioner's brief, p. 7). Although the amount actually reported by a taxpayer on its Federal tax return may not reduce its taxable income below zero (pursuant to IRC § 172[b][2]), the deduction "allowed" by section 172(a) can be greater than the amount actually reported on the Federal return. Petitioner claims that the Administrative Law Judge failed to address petitioner's claim or to consider the distinction between the NOL deduction allowed under Tax Law § 208(9)(f) (and IRC § 172) and the NOL deduction which a taxpayer utilizes on its Federal tax return. Finally, petitioner argues that the recent decision of this Tribunal in Matter of Brooke-Bond Group (Tax Appeals Tribunal, December 28, 1995) supports petitioner's position that the New York NOL deduction can be greater than the amount claimed on the Federal return since Brooke-Bond has "effectively decoupled New York NOL deductions from federal deductions" (Petitioner's supplemental brief, p. 7) and "has clearly endorsed the proposition that a New York taxpayer's NOL deduction can also be greater than its federal deduction so long as it does not exceed the allowable federal net operating loss" (Petitioner's supplemental response, p. 3).

The Division, in opposition, argues that the Administrative Law Judge correctly determined that the amount of the NOL deduction claimed by a taxpayer on its New York State corporate franchise tax return is limited to the amount of such deduction actually reported on its Federal corporation income tax return. The Division argues that in order to correctly interpret Tax Law § 208(9)(f), each of the words contained therein is significant, not just the word "allowed" as argued by petitioner. The Division argues that this issue has been decided previously by the former State Tax Commission, this Tribunal and the Courts of the State of New York in favor of the Division's position and against the interpretation urged by petitioner. The Division argues that the Tribunal's recent decision in Matter of Brooke-Bond Group (supra) also supports the Division's position in the current matter.

We agree with the determination of the Administrative Law Judge.

Tax Law § 208(9)(f), in the applicable part, provides that:

> "A net operating loss deduction shall be allowed which shall be presumably the same as the net operating loss deduction allowed under section one hundred seventy-two of the internal revenue code . . . .
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> "(3) such deduction shall not exceed the deduction for the taxable year allowed under section one hundred seventy-two of the internal revenue code . . . ."

Section 172(a) of the Internal Revenue Code provides:

> "There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term 'net operating loss deduction' means the deduction allowed by this subsection."

Section 172(b) of the Internal Revenue Code provides, in relevant part, as follows:

> "(2) AMOUNT OF CARRYBACKS AND CARRYOVERS.--The entire amount of the net operating loss for any taxable year (hereinafter in this section referred to as the 'loss year') shall be carried to the earliest of the taxable years to which (by reason of paragraph [1]) such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. For purposes of the preceding sentence, the taxable income for any such prior taxable years shall be computed--

> (A) with the modifications specified in subsection (d) other than paragraphs (1), (4), and (5) thereof, and
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> (B) by determining the amount of the net operating loss deduction without regard to the net operating loss for the loss year or for any taxable year thereafter,
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> and the taxable income so computed shall not be considered to be less than zero."

Petitioner argues that use of the term "allowed" in Tax Law § 208(9)(f) requires that the New York NOL deduction only be limited by the amount of the aggregate NOL carryovers and NOL carrybacks calculated (i.e., "allowed") for Federal purposes. This position is not correct. Petitioner gives undue importance to the term "allowed" and fails to read it in the context of IRC § 172. The issue for decision is not the scope of the word "allowed." What must be determined is the amount of the NOL that may be deducted on the New York State corporate franchise tax return for a given year. Petitioner concedes this at page 15 of its brief in support: "Refco does not deny that the present matter ultimately concerns the amount of the NOL deduction which Refco may claim" (Petitioner's brief, p. 15).

The Federal NOL deduction is premised on allowing losses that exceed taxable income in a particular year to be carried back and forward as necessary to offset taxable income in other years. This requires a mechanism to calculate such excess losses. Thus, IRC § 172(a) allows a deduction for the aggregate NOL carryovers and carrybacks for a taxable year. This is borne out by the Federal regulation section 1.172-1(b) providing the steps for computation of the NOL deduction. This aggregate NOL deduction is then carried back or forward as provided in section 172(b)(1). To the extent that it exceeds taxable income in the carryback or carryforward years, it continues to be carried back or forward until exhausted or until it is beyond the periods provided in section 172(b)(1). If section 208(9)(f) of the Tax Law provided that the New York State NOL was presumably the same as the NOL deduction allowed under IRC § 172(a), petitioner would have a stronger base for its argument. However, Tax Law § 208(9)(f) provides that a NOL deduction shall be allowed which is presumably the same as that allowed under IRC

§ 172, not just section 172(a). Therefore, the limitation of the amount of NOL carryovers and carrybacks contained in section 172(b)(2) must also be considered.

As the Administrative Law Judge concluded:

> "[t]he ordering rule in section 172(b)(2) of the Code limits the Federal NOL deduction when it provides that Federal taxable income must not be considered to be less than zero. Thus, the deduction allowed in a particular year will not be more than Federal taxable income in that year. The excess portion of a potential Federal NOL deduction that is more than Federal taxable income cannot be used for that year because there is no Federal taxable income against which to apply the excess portion of the NOL carrybacks and carryforwards. Section 172 of the Code specifically says that Federal taxable income cannot be taken below zero" (Determination, conclusion of law "E").

Petitioner argues that its situation is distinguishable from that of the taxpayer in Royal Indemnity, which was relied on by the Administrative Law Judge. Although there are factual differences between Royal Indemnity and the present case, these factual differences do not require a different conclusion. In Royal Indemnity, the Court of Appeals affirmed the decision of this Tribunal in which we considered the taxpayer's argument that the NOL deduction is limited only by Federal computational provisions. The taxpayer attempted to carry forward losses for State purposes from a year for which it had already claimed such losses on its Federal return. Petitioner in the present case argues that since such losses were no longer "allowed" to be used on the taxpayer's Federal return, the Court properly denied their deduction for New York purposes. However, the Court of Appeals did not base its decision on whether the losses were allowable for Federal purposes in the year at issue. Rather, it found that "in 1976 and 1977 the amount of the deduction petitioner took for net operating losses for State tax purposes was greater than the amount taken for Federal tax purposes" and concluded that "the New York net operating loss deduction cannot exceed the amount deducted on the Federal return for the corresponding year" (Matter of Royal Indemnity Co. v. Tax Appeals Tribunal, supra, 550 NYS2d 610, 611). As a result, we believe that the Administrative Law Judge correctly relied on Royal Indemnity as being dispositive of this case.

In our decision in Matter of Royal Indemnity Co. (Tax Appeals Tribunal, February 19, 1988), we concluded that the use in the State statute of the word "allowable" means "the amount of the federal deduction necessary to reduce Federal taxable income to zero." We stated:

> "[f]inally, one rationale underlying Sheils, [Matter of Sheils v. State Tax Commn., 52 NY2d 954, 437 NYS2d 968] that the taxpayer not benefit from a double deduction, supports this interpretation of 'allowable.' If the petitioner's State net operating loss deduction was not limited to the amount actually absorbed on the corresponding Federal return, the petitioner would potentially benefit from the same deduction twice on its State return. This could occur since the excess would be deducted on the State return in one year, but could be carried forward or backward for Federal purposes to another year. This carryover to another year for Federal purposes would result in the same amount appearing as a Federal net operating loss deduction apparently qualifying as a State deduction for a second time. Since the Division's interpretation of 'allowable' prevents such double deductions, it is neither irrational nor unreasonable and should be upheld" (Matter of Royal Idemnity Co., supra).

This rationale is equally applicable to petitioner in the present case.

Contrary to petitioner's argument, our recent decision in Matter of Brooke-Bond Group (supra) does not support petitioner's case. In Brooke-Bond, we considered whether, if New York State entire net income is smaller than Federal taxable income before taking the NOL deduction, a taxpayer should be allowed to take a smaller loss deduction for New York State purposes than it did for Federal purposes. The taxpayer's interest in doing so was to retain the unused NOL in order to carry it forward in later years. In that case, we stated:

> "[i]t seems clear that the Legislature anticipated that, in some situations, the New York State NOL would exceed the Federal NOL. In those cases, the Legislature specifically provided that the New York State NOL deduction could not exceed the Federal deduction for a particular year (Tax Law § 208[9][f][3]). However, there is no corresponding provision in Tax Law § 208(9)(f) that provides that the New York State NOL deduction can never be less than the Federal deduction.
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> ". . . Petitioner has met the requirement that in each of the years at issue its New York State NOL deduction did not exceed its Federal NOL deduction. Further, for each year at issue, the amounts of NOL petitioner carried forward for its New York State NOL deduction were from the same source year(s) and in a lesser amount than that which comprised the Federal NOL deduction (see, Aetna Casualty & Surety Co. v. Tax Appeals Tribunal, 214 AD2d 238, 633 NYS2d 226, lv denied ___ NY2d ___ [Mar. 28, 1996]). No basis appears for requiring a taxpayer to calculate a negative New York State entire net income in a year when its Federal NOL deduction exceeds

> the New York State entire net income for the sole purpose of achieving parity with the Federal NOL deduction" (Matter of Brooke-Bond Group, supra).

Unlike Brooke-Bond, there is a provision in Tax Law § 208(9)(f) that provides that the New York State NOL deduction can never exceed the allowable Federal NOL deduction for a particular taxable year. Therefore, Brooke-Bond does not support petitioner's argument.

It must be remembered that in administrative hearings before the Division of Tax Appeals, the petitioner generally bears the burden of proof (20 NYCRR 3000.15[d][5]). Further, the petitioner bears the burden of demonstrating his entitlement to a claimed exemption or deduction "by demonstrating that the only reasonable interpretation of applicable law so provides him" (Matter of Howes v. Tax Appeals Tribunal, 159 AD2d 813, 552 NYS2d 972).

> "When . . . it is undisputed that the taxpayer's income is subject to the taxing statute, but he claims an exemption from taxation . . . the party claiming [the exemption] must be able to point to some provision of law plainly giving the exemption [citations omitted]. Indeed, if a statute or regulation authorizing an exemption is found, it will be 'construed against the taxpayer'. . . . This is because an exemption is not a matter of right, but is allowed only as a matter of legislative grace. . . .
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> "A deduction is functionally a particularized species of exemption from taxation. . . . The burden is on the taxpayer seeking the deduction to establish his right to it" (Matter of Grace v. New York State Tax Commn., 37 NY2d 193, 371 NYS2d 715, 718-719).

As with the taxpayer in Royal Indemnity, petitioner herein has not met its burden to show that its interpretation of section 208(9)(f) is correct or that the interpretation of the Division is erroneous.

Accordingly, it is ORDERED, ADJUDGED and DECREED that:

1. The exception of Refco Properties, Inc. is denied;

2. The determination of the Administrative Law Judge is sustained; and

3. The petition of Refco Properties, Inc. is denied.

DATED: Troy, New York
July 11, 1996

/s/Donald C. DeWitt
Donald C. DeWitt
President

/s/Francis R. Koenig
Francis R. Koenig
Commissioner